

## PHU NHUAN JEWELRY JSC (PNJ) - UPDATE

<b>Market Price</b> VND81,600	<b>Target Price</b> VND86,200	<b>Dividend Yield</b> 2.2%	<b>Rating</b> HOLD	<b>Sector</b> CONSUMER GOODS
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### Outlook – Short term



### Outlook – Long term



### Valuation



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### Key changes in the report

- FY20 net profit decreased by 9.4%

### Price performance



Source: VND RESEARCH

### Key statistics

52w high (VND)	92,500
52w low (VND)	70,262
3m Avg daily volume (shares)	705,611
3m Avg daily value (VNDm)	60,532
Market cap (VNDbn)	18,379
Outstanding shares (m)	225
Free float (%)	80
TTM P/E (x)	15.3
Current P/B (x)	4.0

### Ownership

Cao Thi Ngoc Dung	9.0%
LGM Investments Ltd	4.4%
Route One Investment Company	3.9%

Source: VND RESEARCH

## Fire tests true gold

**FY19 net profit within our expectation.** PNJ witnessed a 16.7% yoy rise in the top line and a 24.1% yoy increase in the bottom line thanks to a 1.3% pts expansion of gross margin to 20.4%. Accordingly, the FY19 results came at in 103.6% and 102.9% of our revenue and net profit forecasts, respectively.

**Covid-19 outbreak might dent topline in near-term.** We believe that PNJ's 1H20F earnings are likely to be dampened by subdued demand for discretionary products as a result of the COVID-19 outbreak. We observe that the outbreak has started to hurt the wholesale segment since Jan 2020 as shop owners hesitated to stock up jewellery products. We expect the cautious sentiment to spread to the retail segment since mid-1Q20F as consumers become less eager to spend on discretionary products.

**We lower our FY20F forecasts to factor in the weak demand.** We cut our FY20F net revenue/net profit forecasts by 3.9%/9.4%, respectively, on the backdrop of 1) lower sales of both retail/wholesale segment (-6.6%/-7.4% vs. old forecast); and 2) a slower-than-expected store openings schedule (only 20 PNJ Gold stores in FY20F vs. 25 in previous forecast). As the outbreak is controlled, we expect PNJ to post 16.5% yoy growth in net profit in FY21F on the back of further store openings (+20 stores) and a 0.4% pts expansion in gross margin.

**Reiterate HOLD rating with lower TP of VND86,200.** We trim our DCF-based target price by 2.0% following a 13.3% downward revision in FY20F EPS. Per our observation, despite the upward trend of gold price, PNJ's share price still slid to reflect market's view on the future prospects of PNJ amid COVID-19.

**Risk and re-rating catalyst:** Potential re-rating catalysts include 1) a faster-than-expected store opening, 2) an improvement in consumer sentiment, and 3) new projects to bolster sales. Downside risk is the prolonged COVID-19 outbreak.

Financial summary (VND)	12-18A	12-19A	12-20E	12-21E
Net revenue (bn)	14,573	17,001	18,440	19,953
Revenue growth	32.8%	16.7%	8.5%	8.2%
Gross margin	19.1%	20.4%	20.5%	20.9%
EBITDA margin	9.0%	9.8%	10.4%	11.1%
Net profit (bn)	960	1,191	1,408	1,639
Net profit growth	32.4%	24.1%	18.2%	16.4%
Recurring profit growth	33.1%	24.3%	18.3%	16.5%
Basic EPS	4,312	5,349	6,250	7,275
Adjusted EPS	3,885	4,891	5,770	6,769
BVPS	16,819	20,303	24,750	30,232
ROAE	28.7%	28.6%	27.7%	26.5%

Source: VND RESEARCH

**FY19 review: Full recovery in 4Q19**

**PNJ showed full recovery from the ERP incidents and ramped up store opening in 4Q19.** According to PNJ, the enterprise resource planning (ERP) system has stabilised, helping to optimise production capacity, and the company will return to the expansion pace after a slowdown in 3Q19 due to the ERP issue. In 4Q, PNJ opened 10 new PNJ Gold stores and closed down 9 PNJ Silver stores, bringing the total stores opened in FY19 to 30, yet still fell short of the 40/35 stores assumed in our estimates/PNJ's guidance for FY19. Furthermore, the company has introduced new products to cater to demand in the wedding season and festivals, including the Disney-themed collection following a partnership agreement between PNJ and Walt Disney. Accordingly, retail/wholesale jewelry sales increased 30%/11% yoy in 4Q19.

Figure 1: PNJ's collaboration with Walt Disney



Source: VNDIRECT RESEARCH, COMPANY WEBSITES

Figure 2: A new PNJ NEXT store in Da Nang opened in 4Q19



Source: VNDIRECT RESEARCH, WEBSITES

Figure 3: FY19 results review

FYE (VNDbn)	4Q18	4Q19	% yoy	FY2018	FY2019	% yoy	vs. FY19 forecast	Comments
<b>Net revenue</b>	<b>4,063.4</b>	<b>5,321.3</b>	<b>31.0%</b>	<b>14,571.1</b>	<b>17,000.6</b>	<b>16.7%</b>	<b>103.6%</b>	Broadly in line with our forecast, driven by a jewellery revenue rise of 17.3% yoy in FY19, thanks to 1) retail sales that grew 17% yoy in FY19 (+30 PNJ Gold stores), with a 4Q19 rebound of 30.0% yoy after the ERP incident in 2Q19, and 2) gold bar sales jumping 34.0% yoy thanks to a bolstered demand amid strong gold price fluctuation.
<i>Jewellery revenue</i>	<i>3,969.5</i>	<i>5,304.6</i>	<i>33.6%</i>	<i>14,429.0</i>	<i>16,925.0</i>	<i>17.3%</i>	<i>104.5%</i>	
Gross profit	826.1	1,022.6	23.8%	2,779.1	3,460.7	24.5%	99.9%	Slightly below our forecast on a higher contribution (20.7% of total sales) of the low-margin gold bar segment (vs. 19.0% in our forecast)
<b>Gross profit margin</b>	<b>20.3%</b>	<b>19.2%</b>	<b>-1.1% pts</b>	<b>19.1%</b>	<b>20.4%</b>	<b>+1.3% pts</b>	<b>-0.7% pts</b>	
Selling expenses	351.5	367.6	4.6%	1170.1	1362.6	16.5%	93.8%	
<i>as % of revenue:</i>	<i>8.7%</i>	<i>6.9%</i>	<i>-1.8% pts</i>	<i>8.0%</i>	<i>8.0%</i>	<i>+0.0% pts</i>	<i>-0.9% pts</i>	
G&A expenses	118.6	133.6	12.6%	345.9	479.1	38.5%	101.7%	
<i>as % of revenue:</i>	<i>2.9%</i>	<i>2.5%</i>	<i>-0.4% pts</i>	<i>2.4%</i>	<i>2.8%</i>	<i>+0.4% pts</i>	<i>-0.1% pts</i>	
Operating profit	335.4	480.8	43.4%	1,203.6	1,502.2	24.8%	97.4%	
Pre-tax profit	336.1	481.3	43.2%	1,205.6	1,502.7	24.6%	103.8%	
<b>Net profit</b>	<b>265.5</b>	<b>384.8</b>	<b>44.9%</b>	<b>959.9</b>	<b>1,190.7</b>	<b>24.0%</b>	<b>102.9%</b>	In line with our forecast
Net margin	6.5%	7.2%	+0.7% pts	6.6%	7.0%	+0.4% pts	-0.1% pts	

Source: PNJ, VNDIRECT RESEARCH

### Jan 2020 update showed mixed results amid COVID-19 impacts

In PNJ's January business report, PNJ sustained a 16.5% yoy growth in retail sales but recorded a significant decline of 32.0% yoy in wholesale revenue.

**Retail sales received positive news.** Retail sales (accounting for 65.4% of total sales in Jan 2020) was bolstered by 16.5% yoy thanks to 1) further introduction of new collections for Tet holiday, 2) ticket size growing 10% yoy, 3) the stores opened in Jan 2019 that posted a 40% yoy growth in sales on average, with the fastest pace observed in new stores in Ho Chi Minh City and Southwestern provinces, and 4) the watch segment that has boosted sales by six times vs. Jan 2019, driven by 26 watch stores opened in 2019.

**Wholesale segment was first to get hit by the COVID-19 outbreak.** PNJ's wholesales revenue (making up 18.0% of the total Jan 2020 revenue) has plummeted 32.0% yoy due to 1) an export disruption due to extended public holidays, 2) clients' low stock demand as gold price reached a record high level, and 3) clients' subdued sentiment as they expected a lack of demand for luxury products.

### FY20F outlook: Dampened sales following subdued sentiment

**We lower FY20 forecasts to factor in dampened sentiment.** We expect the virus outbreak to further weaken PNJ's sales in both retail and wholesale platforms. Henceforth, we cut our FY20F net profit forecasts by 9.4% due to expected weaker sales as a result of the COVID-19 outbreak and the continued weak consumer sentiment in PNJ's key markets (Hanoi and HCMC). Particularly, we revised downward retail/wholesale revenue by 6.6%/7.4% respectively, vs. previous forecasts due to 1) the average revenue growth per store being trimmed to 2.0% yoy in FY20F (vs. 5.0% in old forecast), 2) a slowdown in store opening, with just 25 PNJ Gold stores expected (vs. 30 stores in old forecast), and 3) a plunge in shopowners' demand amid COVID-19 fears. On the other hand, we estimate that the gold bar segment will increase its contribution in PNJ's total sales to 22.0% (vs. 19.2% in previous forecast) thanks to the higher demand for gold bar amid cautious sentiment about the world economy.

Figure 4: Earnings revision

	2020F			2021F	Comments
	Old	New	%Δ		
<b>Net revenue</b>	<b>19,189</b>	<b>18,440</b>	<b>-3.9%</b>	<b>19,953</b>	We adjust downward our FY20 net revenue forecast to reflect our estimates in 1) the impact of COVID-19 outbreak, with the average revenue growth forecast trimmed to 2%
Retail revenue	11,646	10,876	-6.6%	12,333	yoy in FY20F (vs. 5% yoy in our old forecast), and 2) a slowdown in store opening, as
Wholesale revenue	3,289	3,046	-7.4%	2,698	just 25 PNJ Gold stores are expected to be launched (vs. 30 stores in our old
Gold bar revenue	3,144	3,942	25.4%		forecast)
<i>Net revenue growth</i>	<i>12.9%</i>	<i>16.7%</i>		<i>8.2%</i>	
Gross profit	4,090	3,782	-7.5%	4,162	We slightly downgrade PNJ's blended GPM due to a lower contribution of high-margin gemstone jewellery in response to the decline in demand as PNJ penetrates into tier-2 cities, and a higher contribution of the low-margin gold bar segment
<b>Gross profit margin</b>	<b>21.3%</b>	<b>20.5%</b>	<b>-0.8% pts</b>	<b>20.9%</b>	
Selling expenses	1,552	1,521	-2.0%	-1,603	
as % of revenue:	8.1%	8.2%	+0.1% pts	-8.0%	
G&A expenses	484	408	-15.7%	430	
as % of revenue:	2.5%	2.2%	-0.3% pts	2.2%	
Operating profit	2,054	1,853	-9.8%	2,129	
EBT	1,943	1,760	-9.4%	2,050	
Net profit	1,554	1,408	-9.4%	1,639	
<i>Net margin</i>	<i>8.1%</i>	<i>7.6%</i>	<i>-0.5% pts</i>	<i>8.2%</i>	

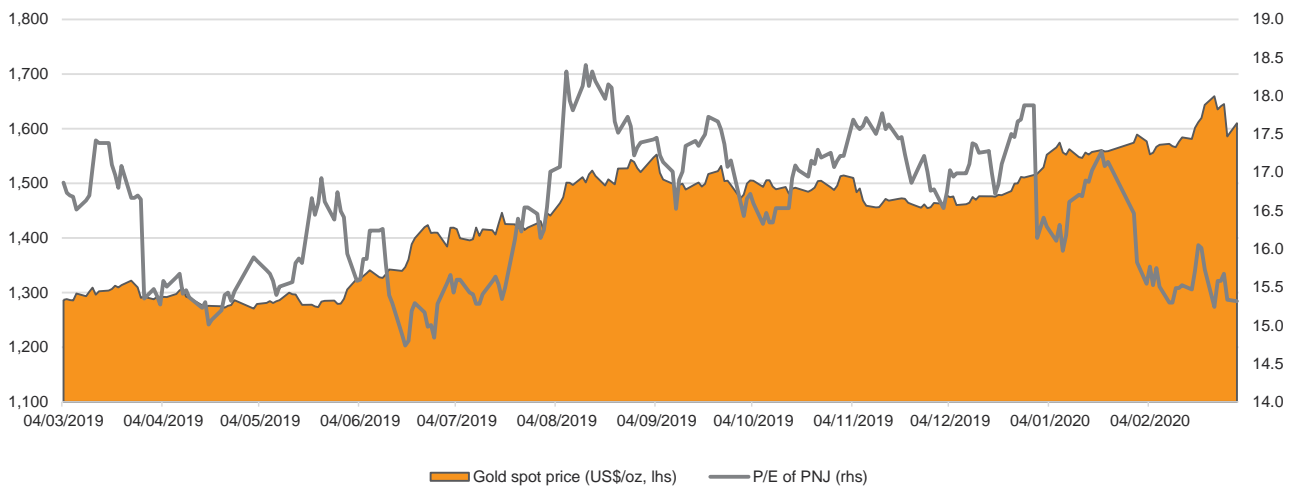
Source: VNDIRECT RESEARCH

We also expect PNJ to continue to register 8.2% yoy and 16.4% yoy growth in net revenue and net profit in FY21F, respectively, on the back of 1) average revenue growth per gold store of 3.0%/year and average revenue per silver store of 2.0%/year, 2) 20 new stores to be launched in FY21F and 3) a 0.4% pts gross margin expansion to 20.9% in FY21F thanks to the continuous inclusion of more high-margin gemstone products.

**Valuation**

**PNJ’s share price needs more than the support of gold price.** Since PNJ is a jewellery manufacturer and retailer, its share price is perceived to be influenced by gold price movement. Per our observation (Figure 5), PNJ’s P/E largely moves in the same direction as gold price but it has displayed a negative correlation since the beginning of this year when gold price rose but PNJ’s P/E slipped amid the COVID-19 outbreak. We believe that, despite the upward trend of gold price, PNJ’s P/E still reflects the market’s sentiment about its core business and future prospects. PNJ is currently trading at TTM P/E of 15.3x and our target price would translate into FY20F P/E forward of 13.8x.

Figure 5: The movements of global gold price and PNJ’s P/E multiple (1-year horizon)



Source: BLOOMBERG, VNDIRECT RESEARCH

**Reiterate HOLD rating with lower TP at VND86,200.** We revised downward our FY20F EPS by 13.3% and our EBIT FY20-29F CAGR to 8.7% (vs. 8.9% in previous forecast) due to the impact of the outbreak and consumers’ caution about the global economy. Accordingly, we trim our DCF-based target price to VND86,200 and reiterate HOLD rating on PNJ. Potential re-rating catalysts include 1) a faster-than-expected store opening, 2) an improvement in consumer sentiment, and 3) new projects to bolster sales. Downside risk to our call is the prolonged COVID-19 outbreak.

**Figure 6: Discounted Cash Flow (DCF Valuation)**

DCF Valuation	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
EBIT	1,853	2,129	2,393	2,631	2,929	3,116	3,307	3,595	3,758	3,928	4,359
Tax	-353	-411	-463	-509	-568	-605	-642	-699	-731	-765	-876
Depreciation	56	73	91	110	127	146	168	184	202	222	244
Capex	-364	-394	-433	-360	-414	-476	-364	-400	-440	-484	-531
Change in working cap	-397	-181	-1,137	-269	-223	-180	-202	4	2	-13	83
Free Cash Flows	795	1,216	451	1,603	1,851	2,001	2,267	2,684	2,791	2,888	3,279
Present Value of FCF	652	900	307	978	1,018	1,001	1,043	1,100	1,033	982	1,016

Source: VNDIRECT RESEARCH

**Figure 7: Assumptions**

Cost of Capital	Current
Beta	0.9
Market Risk Premium	10.1%
Risk Free Rate	4.0%
Cost of Equity	13.5%
Cost of Debt	5.5%
Corporate Tax Rate	20.0%
WACC	10.3%

Source: VNDIRECT RESEARCH

**Figure 8: Target valuation**

DCF Method	Amount	Unit
PV of Free Cash Flows	9,014	VNDbn
PV of Terminal Value (2.0% growth)	12,913	VNDbn
<b>Enterprise value</b>	<b>21,927</b>	<b>VNDbn</b>
Cash and cash equivalents	95	VNDbn
Total debts	(2,615)	VNDbn
Equity Value	19,408	VNDbn
Shares	225	million
<b>Price per share</b>	<b>86,200</b>	<b>VND/share</b>

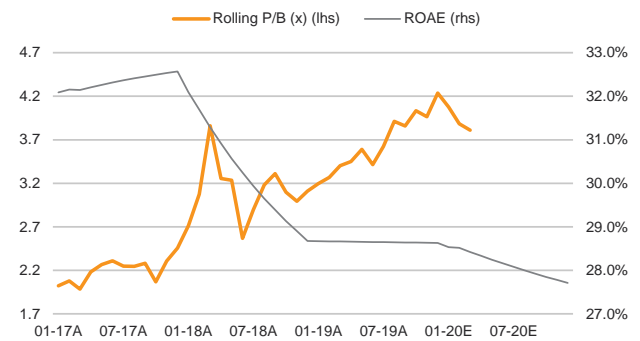
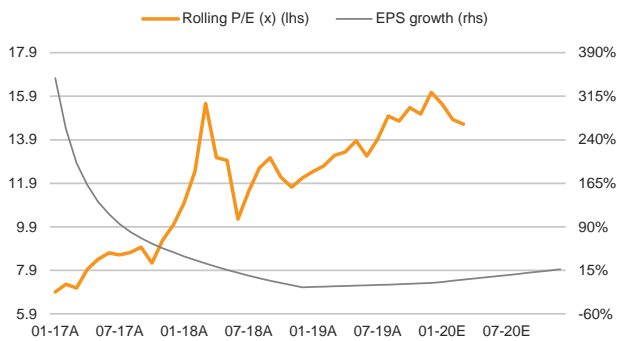
Source: VNDIRECT RESEARCH

**Figure 9: Peer Comparison**

Company	Ticker	Recom.	Target Price (VND)	Market Cap (US\$ m)	EPS growth (%)		P/E (x)		P/B (x)		ROE (%)		ROA (%)	
					FY20F	FY21F	FY20F	FY21F	FY20F	FY21F	FY20F	FY21F	FY20F	FY21F
Tiffany & Co	TIF US	NA	NA	16,172	-3.2	6.1	29.1	27.4	5.0	4.7	18.37	18.64	NA	12.20
Chow Tai Fook Jewellery Group Ltd	1929 HK	NA	NA	8,918	-4.1	23.1	15.1	12.3	2.1	2.0	15.0	17.0	8.3	9.7
Chow Sang Sang Holdings International Ltd	116 HK	NA	NA	798	6.4	11.1	6.0	5.4	0.5	0.5	9.1	9.2	7.5	7.5
LEYSEN Jewelry Inc	03900 CH	NA	NA	396	4.4	16.7	16.5	14.2	1.0	1.0	8.3	8.4	NA	NA
<b>Average</b>				<b>6,571</b>	<b>0.9</b>	<b>14.3</b>	<b>16.7</b>	<b>14.8</b>	<b>2.2</b>	<b>2.1</b>	<b>12.7</b>	<b>13.3</b>	<b>7.9</b>	<b>9.8</b>
<b>Median</b>				<b>4,858</b>	<b>0.6</b>	<b>13.9</b>	<b>15.8</b>	<b>13.3</b>	<b>1.6</b>	<b>1.5</b>	<b>12.0</b>	<b>13.1</b>	<b>7.9</b>	<b>9.7</b>
Phu Nhuan Jewelry JSC	PNJ VN	HOLD	86,200	809	16.8	16.4	13.6	11.8	3.3	2.7	26.5	24.6	14.7	14.2

Source: BLOOMBERG, VNDIRECT RESEARCH (DATA AS AT 02/03)

**Valuation**



**Income statement**

(VNDbn)	12-19A	12-20E	12-21E
Net revenue	17,001	18,440	19,953
Cost of sales	(13,540)	(14,658)	(15,791)
Gen & admin expenses	(479)	(408)	(430)
Selling expenses	(1,363)	(1,521)	(1,603)
<b>Operating profit</b>	<b>1,619</b>	<b>1,853</b>	<b>2,129</b>
Operating EBITDA	1,675	1,909	2,202
<b>Depreciation and amortisation</b>	<b>(56)</b>	<b>(56)</b>	<b>(73)</b>
<b>Operating EBIT</b>	<b>1,619</b>	<b>1,853</b>	<b>2,129</b>
Interest income	2	9	9
Financial expense	(119)	(102)	(88)
Net other income	1	0	(1)
Income from associates & JVs	0	0	0
<b>Pre-tax profit</b>	<b>1,503</b>	<b>1,760</b>	<b>2,049</b>
Tax expense	(312)	(352)	(410)
Minority interest	0	0	0
<b>Net profit</b>	<b>1,191</b>	<b>1,408</b>	<b>1,639</b>
Adj. net profit to ordinary	1,191	1,408	1,639
Ordinary dividends	(344)	(406)	(406)
<b>Retained earnings</b>	<b>847</b>	<b>1,002</b>	<b>1,233</b>

**Balance sheet**

(VNDbn)	12-19A	12-20E	12-21E
Cash and equivalents	95	271	476
Short term investments	0	0	0
Accounts receivables	138	171	189
Inventories	7,019	7,049	7,429
Other current assets	78	149	122
<b>Total current assets</b>	<b>7,330</b>	<b>7,640</b>	<b>8,216</b>
Fixed assets	923	1,232	1,551
Total investments	0	0	0
Other long-term assets	346	349	355
<b>Total assets</b>	<b>8,599</b>	<b>9,221</b>	<b>10,122</b>
Short-term debt	2,611	1,844	1,596
Accounts payable	688	361	576
Other current liabilities	719	1,431	1,132
<b>Total current liabilities</b>	<b>4,018</b>	<b>3,636</b>	<b>3,304</b>
Total long-term debt	4	4	4
Other liabilities	3	5	3
Share capital	2,253	2,253	2,253
Retained earnings reserve	1,042	1,987	3,161
<b>Shareholders' equity</b>	<b>4,574</b>	<b>5,576</b>	<b>6,811</b>
Minority interest	0	0	0
<b>Total liabilities &amp; equity</b>	<b>8,599</b>	<b>9,221</b>	<b>10,122</b>

**Cash flow statement**

(VNDbn)	12-19A	12-20E	12-21E
<b>Pretax profit</b>	<b>1,503</b>	<b>1,760</b>	<b>2,049</b>
Depreciation & amortisation	56	56	73
Tax paid	(291)	(352)	(410)
Other adjustments	(186)	(10)	(6)
<b>Change in working capital</b>	<b>(1,757)</b>	<b>261</b>	<b>(449)</b>
<b>Cash flow from operations</b>	<b>(675)</b>	<b>1,715</b>	<b>1,257</b>
Capex	(208)	(364)	(394)
Proceeds from assets sales	1	1	2
Others	1	0	0
Other non-current assets changes	0	(3)	(6)
<b>Cash flow from investing activities</b>	<b>(206)</b>	<b>(366)</b>	<b>(398)</b>
New share issuance	69	0	0
Shares buyback	(2)	0	0
Net borrowings	1,048	(767)	(248)
Other financing cash flow	(2)	0	0
Dividends paid	(344)	(406)	(406)
<b>Cash flow from financing activities</b>	<b>769</b>	<b>(1,173)</b>	<b>(654)</b>
Cash and equivalents at beginning of period	207	95	271
<b>Total cash generated</b>	<b>(112)</b>	<b>176</b>	<b>205</b>
Cash and equivalents at the end of period	95	271	476

**Key ratios**

	12-19A	12-20E	12-21E
<b>Dupont</b>			
Net profit margin	7.0%	7.6%	8.2%
Asset turnover	2.28	2.07	2.06
ROAA	16.0%	15.8%	16.9%
Avg assets/avg equity	1.79	1.76	1.56
ROAE	28.6%	27.7%	26.5%
<b>Efficiency</b>			
Days account receivable	1.0	1.3	1.4
Days inventory	189.2	176.0	171.7
Days creditor	18.5	9.0	13.3
Fixed asset turnover	20.71	17.11	14.33
ROIC	16.6%	19.0%	19.5%
<b>Liquidity</b>			
Current ratio	1.8	2.1	2.5
Quick ratio	0.1	0.2	0.2
Cash ratio	0.0	0.1	0.1
Cash cycle	171.7	168.3	159.8
<b>Growth rate (yoy)</b>			
Revenue growth	16.7%	8.5%	8.2%
Operating profit growth	28.3%	14.5%	14.9%
Net profit growth	24.1%	18.2%	16.4%
EPS growth	24.1%	16.8%	16.4%

Source: VND RESEARCH

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### RECOMMENDATION FRAMEWORK

#### Stock Ratings

Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

*The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.*

#### Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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